BRIEF IN SUPPORT OF PETITION.

I.

Opinion Below.

The opinion below was reported in abstract form only (305 Ill. App. 488) and appears in full in the petition for leave to appeal (pp. 1-9) which is part of the record (p. 2). The Supreme Court of Illinois denied leave to appeal on October 16, 1940, without any opinion.

II.

Jurisdiction Invoked.

The judgment of the Appellate Court was entered on May 20, 1940 (R. 59), and the Supreme Court of Illinois denied leave to appeal on October 16, 1940.

The statutory provision under which the jurisdiction is invoked is under Section 237b of the Judicial Code as amended by the Act of February 13, 1925, 43 Stat. 936, 937 (28 U. S. C. A. Sec. 344b).

The Federal question was raised by the complaint (R. 28, 36) which also attacked the class action as void for want of jurisdiction (R. 33-34). It was also raised defensively by the plea of *res adjudicata* based on the 77B proceedings (R. 42, 43) and such defense was considered and sustained by the court in its opinion (pp. 5-6).

The authorities believed to sustain the jurisdiction are as follows:

(a) The decision of the Appellate Court made final by the denial of leave to appeal is subject to review here on certiorari.

Minneapolis & St. Paul, et al. v. *Rock,* 279 U. S. 410.

Pennsylvania R. Co. v. *Illinois Brick Co.,* 297 U. S. 447.

(b) The order sustaining the defense of res adjudicata based on the 77B proceedings brings this case within Section 237b for review by certiorari.

Cumberland Glass Co. v. *DeWitt,* 237 U. S. 447.

Indiana v. *Brand,* 303 U. S. 95.

Stoll v. *Gottlieb,* 305 U. S. 165.

We quote the following from the *Cumberland* case *supra* (p. 449):

> "Summing up the defenses made in the state court, the Maryland Court of Appeals said (120 Maryland, 386) 'The defendant interposed three pleas—first that it did not commit the wrong alleged; secondly, limitations; thirdly *res adjudicata,* based upon certain proceedings had in the United States District Court for Maryland, and particularly set out in the pleas!
>
> "The Federal question, which is the basis of jurisdiction here, arises upon the plea of *res judicata* to which a demurrer was sustained in the Maryland court of original jurisdiction which judgment was affirmed by the Court of Appeals. This presents a Federal question because the plea of former judgment in a Federal court adjudicating a right of Federal origin, asserts a right which if denied made the case reviewable here under Sec. 709, Revised Statutes, Sec. 237, Judicial Code. *Deposit Bank* v. *Frankfort,* 191 U. S. 499."

See also Robertson & Kirkham on Jurisdiction of the Supreme Court, page 28, Section 15, Note 12, citing *Nutt* v. *Knut,* 200 U. S. 12, on the proposition that the Federal question may be raised defensively.

(c) The action of the court in sustaining the defense of res adjudicata based on the decree in the alleged class action from which the petitioners were excluded as parties and not fairly represented raised a Federal question as a denial of due process under the Fourteenth Amendment.

Scott v. *McNeal,* 154 U. S. 34.
Simon v. *Southern Railway,* 236 U. S. 115.
Paleo v. *Connecticut,* 302 U. S. 319.
Hansberry v. *Lee,* 85 L. ed. p. 11.

(d) The Federal question was properly raised.

No particular words are necessary to raise the Federal question and the question is sufficiently raised if it appears from the nature of the pleadings that a federal right was before the court for a decision (*St. Louis, et al.* v. *Starbird,* 243 U. S. 592, 597). This appears from the complaint (R. 36, par. 17). It appears from the defense (R. 42, 43) and from the opinion (pp. 5-6).

III.

Statement of the Case.

The bond issue of $1,500,000 executed by the mortgagor corporation was guaranteed by its officers (R. 33) and was further secured by preferred stock of the Harris Brothers Company of a par value of $845,600 (R. 1, 2) under an express trust to enforce the guarantee and

the pledge (R. 3). From 1932 to 1938 the mortgagor defaulted and no action was ever taken by the Trustee to protect the bondholders. The default in interest alone from 1932 to 1938 was about $500,000. Taxes from 1928 to 1938 were unpaid, and they aggregated $267,979.06 (R. 47). The guarantee on the bond issue provided that upon a reduction of the bond issue to $1,000,000 the liability of the guarantors should cease. In order to be released from the guarantee one of the guarantors (M. Rothschild) purchased, subsequent to said default, $143,200 of the defaulted bonds at 10 cents on the dollar and tendered them to the Trustee for cancellation in order to reduce the bond issue to $1,000,000 and be released from the guarantee. He did not tender the unpaid interest of $500,000 nor did he tender the unpaid taxes. An alleged Bondholders' Committee, created by the house of issue, sponsored a plan to give the building to the bondholders, subject to the unpaid taxes, and to release the guarantors from their obligation (R. 4, 5). The Trustee of the bond issue was a party to the Plan acting as the depositary thereunder. This Plan was filed on March 31, 1938, in the 77B proceedings.

On May 25, 1938, the alleged class action was commenced by the Security National Bank, a bondholder, seeking in its original complaint *the enforcement of the guarantee* and to restrain the execution of the release by the Trustee (R. 6). The class representative *about-faced* and amended the action wherein it sought *the authorization of the court for the execution of the release of the guarantee* (R. 7-9). The parties to the class action were the persons who sponsored the release. Petitioner Slocum, *who obtained a judgment* on the guarantee, *was not let in as a party* (R. 31). The other petitioners who objected to the release in the Federal Court were also not made parties. At the date when the Superior Court heard only emergency matters

the parties to that alleged class action presented their agreed decree to the court which released the guarantee and procured the entry of the decree on August 9, 1938 (R. 14-19).

In approving the Reorganization Plan in the 77B proceedings the court specifically provided that the release of the guarantee shall not effect those who will not consent thereto (R. 53). The Committee was instructed to consent merely on behalf of those who favored the release but *not on behalf of those who opposed it.* The decree releasing the guarantee *was pleaded in satisfaction of the judgment obtained by petitioner Slocum on the guarantee* (R. 19).

Petitioners filed their complaint on September 7, 1938, which was amended on February 1, 1939. Among other things it was alleged (R. 20-37) that the decree was procured without jurisdiction in that the petitioners whose interest was adverse to that of the alleged representatives of the class were excluded as parties. It was also alleged that the decree was procured by fraud and collusion between the parties to the proceedings in that the alleged representative of the class about-faced for a consideration (R. 29-30). It also charged malfeasance and misfeasance against the Trustee and the Committee. To this complaint the respondents interposed defenses of *res adjudicata* by virtue of the said decree and also by virtue of the 77B proceedings. These defenses were made under the Civil Practice Act of Illinois by a motion to dismiss under Section 48 (R. 41). The trial court sustained these defenses and dismissed the action on April 10, 1939 (R. 57). Its order was affirmed by the Appellate Court on May 20, 1940 (R. 59) and leave to appeal was denied by the Supreme Court of Illinois on October 16, 1940.

Points Intended to be Urged for Reversal.

1. The interest of the petitioners was adverse to the interest of the alleged representatives of the class action, and the court erred in sustaining the defense of *res adjudicata* based on the void decree to which petitioners were not parties and thereby deprived petitioners of due process of law guaranteed by the Fifth and Fourteenth Amendments to the Federal Constitution.

2. The District Court was without jurisdiction in the 77B proceedings to release the guarantors from their liability and to pass on the liability of the Mortgage Trustee for malfeasance and misfeasance, and the court erred in sustaining the defenses of *res adjudicata* based on the foregoing alleged adjudications.

3. The cause of action against the Committee and the Trustee for malfeasance and misfeasance was not the subject matter in the 77B proceedings, and there was never any adjudication by that court on that issue, and the court erred in sustaining the defense of *res adjudicata* based on the 77B proceeding.

4. Orders and decrees obtained by fraud and collusion or without jurisdiction are subject to collateral attack and may not be pleaded in bar to an action by a stranger to the proceedings, and the court erred in sustaining such a decree in bar to petitioners' action and thereby deprived the petitioners of due process of law.

ARGUMENT.

I.

Petitioners were deprived of due process of law guaranteed by the Fourteenth Amendment by the court which sustained the defense of res adjudicata, based on the decree in the alleged class action, to which petitioners were indispensable parties and were deliberately omitted as parties and not fairly represented.

This court had occasion to reverse the Supreme Court of Illinois which held that a class action was binding on the absent members of the class although they were not fairly represented (*Hansberry* v. *Lee,* decided November 12, 1940, 85 L. ed. p. 11). There this court said:

> "The class suit was an invention of equity to enable it to proceed to a decree in suits where the number of those interested in the subject of the litigation is so great that their joinder as parties in conformity to the usual rules of procedure is impracticable. Courts are not infrequently called upon to proceed with causes in which the number of those interested in the litigation is so great as to make difficult or impossible the joinder of all because some are not within the jurisdiction or because their whereabouts is unknown or where if all were made parties to the suit its continued abatement by the death of some would prevent or unduly delay a decree. In such cases where the interests of those not joined *are of the same class* as the interests of those who are, and where it is considered that the former *fairly represent the latter* in the prosecution of the litigation of the issues in which all have a common interest, the court will proceed to a decree."

In deciding that the alleged class action was improperly pleaded in bar and that thereby the parties were deprived of due process this court said (p. 16):

> "It is one thing to say that some members of a class may represent other members in a litigation where the sole and common interest of the class in the litigation, is either to assert a common right or to challenge an asserted obligation. *Smith* v. *Swormstedt,* 16 How. (U. S.) 288, 14 L. ed. 942, *supra; Supreme Tribe, B. H.* v. *Cauble,* 255 U. S. 356, 65 L. ed. 673, 41 S. Ct. 338, *supra; Groves* v. *Farmers State Bank,* 368 Ill. 35, 12 N. E. (2d) 618. It is quite another to hold that all those who are free alternatively either to assert rights or to challenge them are of a single class, so that any group merely because it is of the class so constituted, may be deemed adequately to represent any others of the class in litigating their interests in either alternative. *Such a selection of representatives for purposes of litigation, whose substantial interests are not necessarily or even probably the same as those whom they are deemed to represent, does not afford that protection to absent parties which due process requires.* The doctrine of representation of absent parties in a class suit has not hitherto been thought to go so far. See *Terry* v. *Bank of Cape Fear* (C. C.) 20 F. 777, 781; *Weidenfeld* v. *Northern P. R. Co.* (C. C. A. 8th) 129 F. 305, 310; *McQuillen* v. *National Cash Register Co.* (D. C.) 22 F. Supp. 867, 873, affirmed in 112 F. (2d) 877, 882; *Brenner* v. *Title Guarantee & T. Co.,* 276 N. Y. 230, 11 N. E. (2d) 890, 114 A. L. R. 1010; *cf. Wabash R. Co.* v. *Adelbert College,* 208 U S. 38, 52 L. ed. 379, 28 S. Ct. 182; *Coe* v. *Armour Fertilizer Works,* 237 U. S. 413, 59 L. ed. 1027, 35 S. Ct. 625. Apart from the opportunities it would afford for the *fraudulent and collusive sacrifice of the rights of absent parties,* we think that the representation in this case no more satisfies the requirements of due process than a trial by a judicial officer who is in such situation that he may have an interest in the outcome of the litigation in conflict

with that of the litigants. *Tumey* v. *Ohio*, 273 U. S. 510, 71 L. ed. 749, 47 S. Ct. 437, 50 A. L. R. 1243." (Italics ours.)

The doctrine announced by this court well applies to the instant case.

The judgments in the instant case upon which the pleas of *res adjudicata* was founded are void "upon principles of natural justice, and under the due process clause of the Fourteenth Amendment." (*Simon* v. *Southern Railway*, 236 U. S. 115, 122.)

(a) There was no common interest between the members of the class and the judgment creditor Slocum.

The original suit of the Security National Bank asked for relief for the benefit of the whole class to *enforce the guaranty.* It alleged (R. 6) that *one creditor obtained a judgment* (without naming the creditor) and that there was danger that other judgments would be entered. It asked, among the relief, to restrain further suits and to restrain action on the judgments already procured. *The rights of Slocum, the judgment creditor, were sought to be affected by that suit.* She was known to the plaintiff, and in order to bind her *it was necessary to join her as a party.* When the plaintiff *about-faced,* and instead of seeking the relief for the benefit of the whole class *sought relief against Slocum to restrain her from enforcing the guaranty, she was an indispensible party.* The suit without such judgment creditor as a party was certainly *without jurisdiction.* The original class suit was commenced to enforce the guaranty for the benefit of the class and the *restraining order was sought against the committee,* against the guarantors and against the successor trustee *from carrying out a scheme to release the guaranty* (R. 6-7). In the amended suit the plaintiff sought *to restrain the*

judgment creditor, to restrain all other bondholders from enforcing the guaranty, aiding the committee and the successor trustee to carry out their plan (R. 10). The Security National Bank, a mere bondholder, *which sought to cancel the guaranty,* was not the representative of Slocum whose rights were adjudicated by a judgment in her favor predicated *on the validity of the guaranty.* Slocum, whose interest was *adverse* to that of the plaintiff in the relief sought by the amended suit was therefore an *indispensable party,* and it was the duty of the plaintiff to join her as a party. Even the Supreme Court of Illinois held in its most recent opinion (*Langson* v. *Goldberg,* 373 Ill. 297) that the right of "a member of a class" to represent the class depended on a "common" interest and common "result sought." *Here the interest was adverse.*

In holding adversely to our contention the opinion says (p. 7):

> "It appears that both Hart and Slocum knew of the pendency of these proceedings; neither, however, made any attempt to vacate the decree or appeal from it."

The record shows that Slocum asked leave to intervene prior to the entry of the decree (R. 38). The court denied the request on July 27, 1938 (R. 31), and while she was preparing an amended petition the parties entered the decree on August 9, 1938. She filed her complaint assailing the decree on September 7, 1938 (R. 1). The statement of the court that Hart never sought to vacate the decree *is contradicted by the record* (R. 38). The statement of the court that "Hart, as a depositing bondholder, was represented by the Committee" overlooked that Hart *had objected to the release* in the 77B proceedings (R. 47) and that the order of the Federal Court *expressly forbade the Committee to represent the*

objectors (R. 50). The Committee stated that its actions will not bind those who objected to the release and the Committee was only authorized to act for those who consented to the release (R. 51).

(b) The interest of the dissenters was adverse, and they were known to the parties who fraudulently concealed the proceedings from them.

The decree was similarly *void as to the other bondholders* for the reason that the plaintiff who sought to release the guaranty was not the representative of the bondholders who dissented to the action of the committee and who desired to enforce the guaranty. *They were indispensable parties.* The plaintiff in that suit knew that there were dissenters to the scheme of the committee to release the guaranty, and it *knew* their names and the names of their attorneys. Plaintiff was represented in the 77B proceeding in the hearing before the Federal Master (R. 47). The Security National Bank, the alleged class representative, *knew* that M. A. Rothstein and Irving S. Berman, as attorneys, represented the plaintiff Hart, an objector (R. 47); that the Solvene National Benefit Society was an *objector.* It *knew* the nature of the objections as outlined by the Master (R. 50); that the committee sponsored the scheme and that it held out to the Master that "nothing done here will bind the dissenters." These *dissenters* were depositors (R. 45) whose names were *known,* exclusive of the non-depositors owning bonds in the amount of $130,000 who were *not represented by the Committee.* With the knowledge of these facts, and faced with the express order of the Federal Court that nothing done there should affect the dissenters, *it became the duty of the Security National Bank to make the dissenters parties* or at least to select a group of

n to represent those dissenters. In adjudicating r rights without making them parties *the court d without jurisdiction of the persons of this class, the decree is a nullity as to them.* (*Sheaff* v. *Spind-* 339 Ill. 540; *Chicago Title & Trust Co.* v. *Darley,* 363 197.) The petitioners were deprived of due process *nsberry* v. *Lee,* 85 L. ed. p. 11).

The rights of Slocum as a judgment creditor were affected by the decree to which she was not a party.

s a result of this decree to which Slocum, a judg- nt creditor, was not a party, *she was prevented from enforcement of a judgment after she had gone ough the laborious task of an appeal to the Appellate rt.* This decree to which she was not permitted to be arty was urged in support of a motion in the court ere the judgment was procured to "satisfy the judg- nt," *not by payment,* but by the effect of the decree ich *restrained the enforcement* (R. 19). The execu- n on this judgment was issued August 4, 1938, after disposition of the appeal. The final decree was en- ed within five days, on August 9, 1938. It was en- ed *with great speed* as a levy was threatened, and successor trustee did not await the expiration of rty days for the purpose of an appeal, but *on the t day,* on August 10, 1938, released the guaranty 19). Immediately thereafter a motion was presented the Municipal Court to "satisfy the judgment," *not payment, but by the decree which released the guar- y.* The basis for the satisfaction was (R. 19) "that judgment creditor sought to intervene in that pro- ding on July 27, 1938, and his petition was denied," l the guarantee was released by the decree.

When the plaintiff in the alleged class suit had de- ed to "about face," and instead of seeking relief to

prevent the fraudulent release, to join hands *to aid its accomplishment,* and when it was promised a consideration for such aid, *it ceased to be the representative of the class.* The action was no longer a representative action. The decree which affected the interest of the plaintiffs who were indispensable parties was therefore a *nullity* and could not be pleaded in bar to this action. (*Langson* v. *Goldberg,* 373 Ill. 297.) The decision which held that she had no right to file an independent suit and that her remedy was by a petition to vacate or appeal is in conflict with the decision of this Court in *Simon* v. *Southern Railway,* 236 U. S. 115, 123, holding that one who is not made a party "was not obliged to attack a void judgment in the court that rendered it" but may institute "a new and independent proceeding."

II.

The District Court was without jurisdiction in the 77B proceeding to release the liability of the guarantors as well as the liability of the Trustee and the Committee for malfeasance and misfeasance and the court erred in sustaining the defense of res adjudicata based on the order in the 77B proceeding and thereby petitioners were deprived of due process of law.

In sustaining the defense of *res adjudicata* by reason of the 77B proceeding the opinion states (R. 5):

> "Plaintiffs attack the sale by the trustee of the Harris Brothers stock pledged under the trust deed to the bondholders' committee for $2500; this stock was sold at public auction and the proceeds applied on account of or held for outstanding bonds. The amended complaint contains no allegations as to the actual value of the stock or that the sale price was less than the value or that the trustee was without power to sell. Moreover, this sale was fully described in the Federal court reorganization pro-

> ceedings and after evidence before a master and hearing by the court the sale was confirmed. All questions with reference to the action of the trustee in connection with the Harris Brothers Company stock were finally determined in the Federal court, and its conclusion is a bar to the plaintiffs' claim in this respect."

The court overlooked that *the complaint did not seek to set aside the sale* but to hold the Trustee and the Committee *liable for malfeasance and misfeasance in failing to protect the interest of the bondholders under* their trust duties. The complaint called attention to the specific provisions of the Trust Indenture which provided (R. 3):

> "The trustee is hereby expressly empowered *as a trustee of an express trust,* for and on behalf of all and every of the holders of the bonds hereby secured, to demand and enforce said guaranty and recover upon the same * * * and to make, commence, prosecute * * * all and every such claims * * * actions, suits, and/or proceedings at law or in equity as by the trustee may be deemed appropriate."

Article III of the Trust Deed provided (R. 2) that prior to default the Trustee might deliver proxies to the company to vote the stock *"but this shall be terminated in the event of a default at the election of the Trustee."* Article IV of the Trust Deed called for monthly deposits with the Trustee at the rate of $13,750 per month to be used as a *sinking fund* out of which the Trustee was to set apart the semi-annual interest. The default in the non-payment of taxes was made in 1928 and continued up to the date of the filing of the complaint. There was due for the years 1928 to 1936, $173,905.37, exclusive of penalties (R. 4), and at the date of the reorganization the total aggregate taxes which were ahead of the bond issue amounted to $267,979.06 (R.

47). *The Trustee permitted the default in the monthly deposits and in the interest, aggregating $500,000.* The Trustee did not enter into possession to safeguard the income, and *never foreclosed.* The Trustee *did not take any action on the preferred stock,* with the result *that the preferred stock which had a par value of $845,000 shrank to $2,500.* It stood by and permitted the sale of the assets of the Harris Brothers Company in the year 1936 and to exchange the preferred stock for other stock. Even under the exchange rate in 1936 the new stock was worth $3.00 per share (R. 51) and on *that basis* the shares were then worth about $200,000. As a result of its gross negligence it later produced $2,500! The action was therefore not to set aside the sale but to hold the Trustee liable for its gross neglect (R. 32).

The Committee, in order to prevent action by the bondholders accumulated more than 75 per cent in bonds in its possession and thereby the other bondholders were helpless as under the terms of the Trust Deed no action could be taken by less than 25 per cent (R. 24, 25-26). When a demand was made upon the Trustee to take action the Committee opposed it (R. 26). *The Trustee had no right to stand by and permit the defaults and to refuse to take action on the guaranty because a large majority of bondholders were,* through some device of the Committee, *opposed to such action,* particularly when the Trustee knew of the deal between the Committee and the guarantors to release them from the guaranty. (*Chicago Title & Trust Co.* v. *Chief Wash Co.,* 368 Ill. 146.) The successor trustee was a party to the actions of the Committee as it was *the depositary under the deposit agreement of the Committee.* Its failure to exercise a reasonable discretion, particularly when a demand was made upon it to take such action which caused great loss to the bondholders, constitutes misconduct.

The Appellate Court, in disposing of the action against the Trustee said (p. 8):

> "It is true the trustee permitted defaults in the payment of taxes, but there is no allegation that the trustee could have avoided these faults or had any money to make such payments. There is no allegation that any more could have been realized for the bondholders if the trustee had instituted foreclosure proceedings. The committee, representing 90 per cent of the outstanding bonds, was of the opinion that acceleration and foreclosure were inadvisable. The complaint does not suggest that any greater benefits for the bondholders could have been had than was obtained by them in the reorganization accomplished in the Federal Court."

The complaint alleged (R. 32) that if the Trustee had taken action it would have "collected large funds" from the guarantors who were then "possessed of large funds." The complaint also suggests greater benefit (R. 32-33) if the proper protection was given. All that the bondholders received under the Plan was the real estate which was encumbered with taxes and penalties in excess of $250,000 (R. 4) and subject to the reorganization expenses. The premises could not even earn a sufficient amount to pay the taxes.

III.

The cause of action for malfeasance and misfeasance against the Mortgage Trustee and the Committee was not adjudicated in the 77B proceedings nor was it adjudicated in any of the proceedings, and the court erred in sustaining the defenses of res adjudicata.

The court entirely overlooked that the cause of action for malfeasance and misfeasance of the Mortgage Trustee and of the Committee was not adjudicated in *any* of the proceedings.

(a) The claim against the Trustee was not dischargeable in bankruptcy, and the defense of res adjudicata was improperly sustained.

The claim against the First National Bank which assumed its duties as successor trustee *after default* was not a bankruptcy asset. The claim against the bank was that as Trustee of an "express trust" it was required by law to perform *active* duties and to protect the estate. It allowed the mortgagor to suffer the non-payment of taxes (R. 25) for the years from 1928 to 1936, inclusive, aggregating $173,000 increased up to the date of the reorganization to $267,000. (*People ex rel. Barrett* v. *Central Republic Co.*, 300 Ill. App. 297.) It failed to enforce the guaranty during the time that the guarantors were *solvent,* and failed to vote the preferred stock which was valued in excess of $845,000 and whose valuation shrank to $2,500. The 77B proceedings in no way dealt with that claim, and *the bondholders were not parties to that proceeding for such purpose.* They were parties *for two limited purposes* only: (1) on the reorganization plan, and (2) on the appointment of a trustee. (*Milwaukee-Sawyer Building Corporation,* 79 F. (2) 478; *Trust No. 3988,* 85 F. (2) 942; *Kenmore-Granville Hotel Co.,* 92 F. (2) 778.) The proceedings in 77B were improperly pleaded as *res adjudicata* to the claim against the successor trustee.

(b) The release of the guaranty was not adjudicated in the 77B proceeding, and the court improperly sustained the defense of res adjudicata.

The decree of the Superior Court authorized the Trustee to release the guaranty. This decree was attacked as fraudulent and void. The Trustee interposed the de-

fense of *res adjudicata* by virtue of the 77B proceedings (R. 54). The court sustained such defense. The record conclusively shows that *the Bankruptcy Court did not adjudicate this question in the 77B proceedings but left this matter for determination to the Superior Court of Cook County.* The Federal Master stated in his report (Abst. 50):

> "In this proceeding the Committee is merely asking the approval of the Court for the Committee to consent in the State Court on behalf only of those bondholders who have consented to the plan. The Committee states that nothing done here will bind the dissenters—*that being a matter for the State Court.*"

The Trustee *was not authorized* by the order in the 77B proceedings to release the guaranty. No authority was given to anyone to release the guaranty against those who objected. Hart was an *objector* in the 77B proceeding (Abst. 47). The plaintiff Cohn was a *non-depositor.* Slocum was a judgment creditor. There was no adjudication against them in the 77B proceeding and the defense was erroneously sustained.

IV.

A judgment or decree obtained by fraud and collusion or without jurisdiction is subject to collateral attack and the sustaining of the defenses of res adjudicata based on such a judgment deprived the petitioners of due process of law.

One of the defenses to the action was *that the decree which was assailed for fraud by the complaint was res adjudicata* (R. 54, (2) and (3)). This contention was sustained by the Chancellor who sustained "each and every motion to strike." (R. 57.) Petitioners urged that a decree impeached for fraud may not be pleaded in bar

to the action which assailed it. The Appellate Court held that the decree which was not appealed was properly pleaded in bar. On the record as presented for review *the allegations of the complaint which were confessed to be true were to be considered, and not the facts as they appeared in the fraudulent decree.* (*Railway Express Agency* v. *Jones,* 7 Cir. 106 F. (2d) 341.) Its statement (p. 7) that the Sheboygan Bank's Amended Complaint (where it changed its position) was because of "an investigation of the financial condition of the guarantors" *is based on its allegations and not on petitioners' allegations which assailed the truth thereof.* The matter was disposed of on the motion to dismiss, *which admitted the facts charged in the complaint* that the bank, the alleged class representatives, which filed its first complaint to *restrain the cancellation of the guaranty* and to prevent the acceptance of the $143,200 in bonds (acquired at 10 cents on the dollar) had "about-faced" (R. 7) and filed its Amended Complaint *asking the cancellation of the guaranty and the acceptance of the tender* (R. 30). *The complaint charged that it "about-faced" because of a secret deal,* based on a promise to pay its counsel $1,000, as well as other considerations to the plaintiff (R. 30). It charged that the secret deal was carried out by the entry of the decree (not upon evidence, not upon a reference, and Master's Report, as the Appellate Court says) as an "emergency matter," without *notice to Slocum,* who was then a judgment creditor whose right was sought to be affected. These allegations cannot be overcome by the statement of the court that "mere conclusions as to fraud are not sufficient" as the allegations were ultimate statements of fact.

(a) A decree which is sought to be impeached for fraud cannot be pleaded in bar to the bill of impeachment.

It is elementary that a decree may be impeached for fraud, and *such a decree may not be pleaded in bar to the action.* (*Green* v. *Hutsonville School District,* 356 Ill. 216; *Bernero* v. *Bernero,* 363 Ill. 329.)

(b) The decree was procured by fraud and collusion, and it was the duty of the Appellate Court to reverse the order of dismissal.

On a motion to dismiss the question is presented whether the complaint as a whole states any cause of action, and if it does, no such motion can be sustained. (*Barzowski* v. *Highland Park State Bank,* 371 Ill. 412, 416; *Messick* v. *Mohr,* 292 Ill. App. 69.) The statement (p. 7) that "no facts are shown supporting the charge of fraud and collusion," is refuted by the allegations of the complaint. Paragraph 9 of the complaint charged (R. 29) that after filing the complaint as a class suit for the alleged benefit of the class to prevent the release of the guarantors, the alleged representative of the class, "entered into secret arrangements with the defendants *to obtain the approval* of "the release of the guarantors," and "as part of this scheme it was agreed that the plaintiff would about-face" and file the Amended Complaint seeking therein the cancellation of the guaranty instead of the relief to restrain the cancellation thereof; as an inducement to such class representative to obtain such results it was promised $1,000 for its counsel and other considerations; that the foregoing scheme was carried out (R. 30). The details how it was carried out were stated.

In sustaining the defense that the decree was a bar

to the complaint the court overlooked the rule in *Comstock-Castle Co.* v. *Baldwin,* 169 Ill. 636. There it was said:

> "Courts of equity will not be prevented from protecting the equitable rights of parties by the mere **garb or form in which persons devising fraudulent schemes to obtain the property of others without recompense have clothed their illegal transactions.** The practice of taking advantage of the forms of law and of proceedings of courts of justice to perpetrate such frauds, by organizing fraudulent corporations and by obtaining fraudulent judgments, is by no means uncommon. **To permit laws enacted for the public good to be so perverted and courts of justice to be used and imposed upon, and then to say that there is no remedy because what was done was done under the forms of law,** would be to make the law and the courts themselves the **instrument of dishonest schemers."** (Bold type ours.)

This rule was reiterated by this court in *Pepper* v. *Litton,* 308 U. S. 295.

(1) The decree releasing the guaranty was a result of fraud.

Slocum had a judgment in her favor on the guaranty which was affirmed by the Appellate Court. *The proposition that a guarantor may after default procure a release of the guaranty by the reduction of the bond issue and thereby affect the existing default is such an absurdity that if called to the attention of the Chancellor he would never have stamped the consent decree with his approval.* By their guaranty they agreed to pay *"and and every coupon for interest upon any of said bonds."* (R. 23.) At the date of the entry of the decree *there was a default in interest coupons from January 1, 1932, to July 1, 1938, on the principal amount of $1,143,000.* Here was a clear liability which was due from the

guarantors who were liable thereon without notice or demand (R. 23). The clause (R. 8) that upon the reduction of the bond issue from one and one-half million dollars to one million dollars the guaranty should cease *could not have affected the then existing liability in excess of $500,000 for the default in interest which accrued prior to the reduction.* The entry of the decree *without notice to Slocum* or to any other parties who they knew to be *opposed* to the release *was a fraud upon the court.*

(2) There was no ambiguity in the terms of the trust indenture pertaining to the liability on the guaranty, and the guaranty, and the jurisdiction for the construction of the terms of the trust deed was merely colorable.

A court of equity has jurisdiction to construe a trust when an ambiguity exists and is without jurisdiction to construe a trust when there is nothing to construe. (*Chicago Title & Trust Co.* v. *Robin,* 361 Ill. 261; *Hoefeld* v. *Sixty-third Halsted Realty Co.,* 289 Ill. App. 305.)

In answer to this point the Appellate Court said:

> "Examination of the trust deed (Sec. 13, Art. 5) shows the trustee was authorized to accept and receive in satisfaction of the mortgage debt 'such amount and amounts of money as the trustee in its unlimited discretion may deem advisable.' We find no language specifically authorizing the trustee to accept bonds in compromise of the guaranty. A certain amount of discretion was lodged in the trustee by the terms of the trust deed, but there is no allegation that this discretion was not exercised honestly and fairly."

The fallacy is apparent. *The Trustee refused to exercise its discretion* (R. 13), but relied on the decree, and it is conceded by the court that there is no such power under the terms of the trust. The court also miscon-

ceived the whole point. This was not a case where a payment was made as a consideration for the cancellation of the guaranty and where the question was whether the consideration was sufficient. Here, the Bond Issue was in default and the principal and interest amounted to $1,500,000. By the device of cancelling $143,200 of the defaulted bonds of the principal issue was reduced to $1,000,000, and *thereby* the guarantors were to be relieved from liability. No such discretion was vested in the Trustee, and there is no *legal* basis for the decree. When this matter was presented to the Federal Master he said (R. 50):

> "The committee's representative stated that it may be contended that since the outstanding bonds have been reduced to $1,000,000.00 the guaranty is discharged; that there may be a *question whether that provision of the trust deed applies to liabilities that have accrued.* * * * In this proceeding the Committee is merely asking the approval of the court for the committee to consent in the state court on behalf only of those bondholders who have consented to the plan. The Committee states that *nothing done here will bind the dissenters—that being a matter for the state court.*"

They *did bind the dissenters by the fraudulent decree.*

(3) The release was not the result of a judicial determination in the 77B proceedings.

Neither the Federal Master nor the court in the 77B proceeding *ever passed on the propriety of the release.* The Master merely recommended that the Committee be authorized to consent on behalf of the depositors who did not dissent. The Committee represented to that court *"that nothing done here will bind the dissenters"* and left all matters to the "state court." When action was taken in the Superior Court to "bind the dissenters"

the Committee, the plaintiff, and the Trustee, who had previously agreed on the deal to release the guarantors, should have at least given notice to those who would be affected thereby.

(c) The decree is void for want of jurisdiction and was improperly allowed to be pleaded in bar to the action which sought its avoidance.

It is elementary that *if a court is without jurisdiction of the subject matter or the parties the decree is a nullity and may not be pleaded in bar.* (*People* v. *Miller,* 339 Ill. 573, 588; *Green* v. *Hutsonville School District,* 356 Ill. 216.) We have shown that the court was without jurisdiction of the persons of the petitioners. The sustaining of the defense of *res adjudicata* by virtue of the decree deprived the petitioners of their property without due process of law. (*Scott* v. *McNeal,* 154 U. S. 34; *Simon* v. *Southern Railway,* 236 U. S. 115; *Hansberry* v. *Lee,* 85 L. ed. p. 11.)

V.

The decision that third parties may not file an independent suit to impeach a decree for fraud or to escape the consequences of a void decree and that their remedy is only by appeal or error is contrary to fundamental law and to the decisions of this court.

The opinion pointed out (p. 7) that no appeal or error was sued out and that the decree was not open to collateral attack by the complaint "in the nature of a Bill of Review." It completely overlooked that this was a suit by *third parties* to impeach a decree for fraud which was extrinsic to the record and an independent suit is properly maintainable to attack such a decree. (*Hohrod* v. *State,* 237 Ill. 229; *Bergman* v. *Rhode,* 334

Ill. 143; *Green* v. *Hutsonville School District,* 356 Ill. 216; *Chicago Title & Trust Co.* v. *Darly,* 363 Ill. 197.) In *Bernero* v. *Bernero,* 363 Ill. 328, the court held that a *"third person" may impeach a fraudulent decree by an independent suit.* This court held in *Hansberry* v. *Lee,* 85 L. ed. p. 11 that *a decree for want of jurisdiction is subject to collateral attack.* The decision in the instant case cannot be reconciled with the fundamental law as announced by this court. (*Johnson* v. *Waters,* 111 U. S. 64.)

The Appellate Court completely overlooked the distinction between (1) an independent suit by a third party to impeach a decree for fraud or to avoid the consequences of a void decree, and (2) a bill of review. The *former may even be filed during the pendency of an appeal,* and the only mode to impeach a decree for fraud extrinsic to the record is by an independent suit. In *Dowagiac Mfg. Co.* v. *M'Sherry Mfg. Co.,* 155 F. 524 (C. C. A. 6), the Court said (p. 528).

> "The *radical difference between these two kinds of bills* is that a bill of review is a continuation of the original litigation, whereas *a bill impeaching a decree for fraud is not.* It is new and independent litigation. The rules applicable to the two kinds of bills are different. As, for instance, it is well settled, in certain jurisdictions at least, that a bill of review cannot be filed after a decree has been affirmed on appeal, at least where the ground thereof is newly discovered evidence, unless the right to file it has been reserved in the decree of the appellate court, or permission be given on application to that court directly for that purpose. *Southard* v. *Russell,* 16 How. 545, 14 L. Ed. 1052; 2 Bates on Fed. Eq. Proc. Sec. 717. *But such is not the case as to a bill to impeach a decree for fraud.* It can be filed without such leave being first had. 2 Daniell's Ch. Pl. & Pr. (5th Ed.) 1584; 2 Beach, Mod. Eq. Pr. Sec. 884; *Ritchie* v. *Burke* (C. C.) 109 Fed. 16, 18."

e court further said:

"But *a bill impeaching a decree for fraud need not, in so far as it seeks relief, concern itself with the decree.* It may be limited to seeking an injunction against its enforcement or *to depriving the party in whose favor it has been rendered of the benefit which he has derived from it.* Indeed, it may be that such is all that such a bill is ever properly concerned with. If such a bill is so limited, the above reasoning cannot be applied to prevent its being filed pending on appeal from the decree. The two proceedings are not in such a case seeking the same relief. *The appeal is seeking to have the decree vacated and set aside, whereas the bill is seeking to prevent its enforcement* or to obtain a restoration of the benefits derived under it. It is on the ground that such a bill may be so limited, or such is its proper nature, that it has been held that a Circuit Court of the United States can give relief against a decree of a state court obtained by fraud. It was so held in the cases of *Gaines* v. *Fuentes,* 92 U. S. 10, 23 L. Ed. 524, and *Marshall* v. *Holmes,* 141 U. S. 597, 12 Sup. Ct. 62, 35 L. Ed. 870, where the bills sought an injunction against an enforcement of the decrees, and also in the cases of *Johnson* v. *Waters,* 111 U. S. 667, 4 Sup. Ct. 619, 28 L. Ed. 547, and *Arrowsmith* v. *Gleason,* 129 U. S. 99, 9 Sup. Ct. 237, 32 L. Ed, 630, where the bills sought a restoration of benefits derived under them." (Italics ours.)

The decision was cited with approval in *Peeke* v. *izens Banking Co.,* 81 F. (2) 112, 114 (C. C. A. 6) d in *Irvin* v. *Buick Co.,* 88 F. (2) 947, 949 (C. C. A. 8).

The decision that a judgment assailed for want of isdiction of the person may be pleaded in bar to e action is in conflict with the decision of this court *Simon* v. *Southern Railway,* 236 U. S. 115, 123 and th the "principles of Natural Justice."

It is evident from the foregoing that the decision in

the instant case is *basically unsound* and in *conflict* with "principles of natural justice" and with "due process of law."

For the foregoing reasons we urge the issuance of the Writ.

Respectfully submitted,

MEYER ABRAMS,
LEO L. GINSBURG,
Attorneys for Petitioners.